

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

Financial Statements
with
Independent Auditors' Report
For the years ended December 31, 2012 and 2011

By

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RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Rural Water District No. 2
Jefferson County, Kansas

We have audited the accompanying financial statements of the business-type activities of Rural Water District No. 2, Jefferson County, Kansas as of December 31, 2012 and 2011, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Rural Water District No. 2, Jefferson County, Kansas, as of December 31, 2012 and 2011, and the respective changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in appropriate operational, economic or historical context. However, management has elected to omit this information.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Rural Water District No. 2, Jefferson County, Kansas's financial statements as a whole. The supplemental schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplemental schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional

procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Douthett & Co. CPA, PA

Douthett & Co. CPA, PA

Certified Public Accountants

February 11, 2013

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

STATEMENTS OF NET POSITION
December 31, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|----------------------------------------------------------------|---------------------|-------------------|
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 468,100 | \$ 471,882 |
| Accounts receivable | <u>14,044</u> | <u>11,162</u> |
| Total Current Assets | 482,144 | 483,043 |
| Noncurrent Assets: | | |
| Capital assets, net of accumulated depreciation | 523,593 | 553,155 |
| Bond issue costs, net of accumulated amortization | - | 1,826 |
| Deferred loss on refunding, net of accumulated amortization | <u>-</u> | <u>1,764</u> |
| Total Noncurrent Assets | <u>523,593</u> | <u>556,745</u> |
| TOTAL ASSETS | <u>1,005,737</u> | <u>1,039,789</u> |
| LIABILITIES | | |
| Current Liabilities: | | |
| Accrued expenses | 662 | 490 |
| Customer deposits | 200 | 200 |
| Current portion of revenue bonds payable | <u>-</u> | <u>55,000</u> |
| Total Current Liabilities | 862 | 55,690 |
| NET POSITION | | |
| Invested in capital assets, net of related debt | 523,593 | 498,155 |
| Unrestricted | <u>481,282</u> | <u>485,944</u> |
| TOTAL NET POSITION | <u>\$ 1,004,875</u> | <u>\$ 984,099</u> |

See accompanying notes to financial statements

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

STATEMENTS OF ACTIVITIES
For the years ended December 31, 2012 and 2011

| | 2012 | 2011 |
|---------------------------------------------------|--------------|------------|
| OPERATING REVENUES: | | |
| Water sales | \$ 176,710 | \$ 150,503 |
| New meters | 10,000 | 8,250 |
| TOTAL OPERATING REVENUES | 186,710 | 158,753 |
| OPERATING EXPENSES | 145,938 | 105,376 |
| INCREASE FROM OPERATIONS | 40,772 | 53,377 |
| NONOPERATING REVENUES (EXPENSES) | | |
| Farm income | 21,243 | 3,576 |
| Interest income | 2,086 | 3,914 |
| Other Income | 1,460 | - |
| Amortization expense | (3,590) | (2,534) |
| Depreciation expense | (36,509) | (41,745) |
| Farm expense | (4,686) | (3,947) |
| DECREASE FROM NONOPERATING REVENUES (EXPENSES) | (19,996) | (40,736) |
| INCREASE IN UNRESTRICTED ASSETS | 20,776 | 12,641 |
| NET ASSETS, Beginning of Year | 984,099 | 971,458 |
| NET ASSETS, End of Year | \$ 1,004,875 | \$ 984,099 |

See accompanying notes to financial statements

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

STATEMENTS OF CASH FLOWS
For the years ended December 31, 2012 and 2011

| | 2012 | 2011 |
|--------------------------------------------------------------|------------|------------|
| Cash Flows from Operating Activities: | | |
| Cash received from customers | \$ 183,829 | \$ 163,799 |
| Cash payments to suppliers for goods and services | (109,700) | (71,261) |
| Cash payments to employees for services | (40,753) | (39,290) |
| Other revenues | 24,789 | 7,490 |
| Net Cash Provided by Operating Activities | 58,165 | 60,738 |
| Cash Flows from Capital and Related Financing Activities: | | |
| Purchase of capital assets | (6,947) | (26,423) |
| Repayment of long-term debt | (55,000) | (30,000) |
| Net Cash Used by Capital and Related Financing Activities | (61,947) | (56,423) |
| Net Change in Cash | (3,782) | 4,315 |
| Cash, beginning of year | 471,882 | 467,567 |
| Cash, end of year | \$ 468,100 | \$ 471,882 |

Reconciliation of Operating Income to Net Cash Provided by Operating Activities:

| | | |
|-------------------------------------------------------------------------------------------------|-----------|-----------|
| Change in Net Assets | \$ 20,776 | \$ 12,641 |
| Adjustments to Reconcile Changes in Net Assets to Net Cash Provided by Operating Activities: | | |
| Depreciation | 36,509 | 41,745 |
| Amortization | 3,590 | 2,534 |
| Change in assets and liabilities: | | |
| (Increase) decrease in accounts receivable | (2,882) | 5,046 |
| Increase (decrease) in accrued expenses | 172 | (1,228) |
| Net Cash Provided by Operating Activities | \$ 58,165 | \$ 60,738 |

See accompanying notes to financial statements

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

NOTES TO FINANCIAL STATEMENTS
For the years ended December 31, 2012 and 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Rural Water District No. 2, Jefferson County, Kansas (the District) was organized in 1965 as a quasi-municipal corporation established under and pursuant to the provisions of K.S.A. 82a-612 et seq. of the statutory law of Kansas. The District was established for the purpose of constructing and operating a water supply distribution system to the benefit units within Rural Water District No. 2.

The financial statements of Rural Water District No. 2, Jefferson County, Kansas are prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standard Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (Statements and Interpretations). Governments are also required to follow the pronouncements of the Financial Accounting Standards Board (FASB) issued through November 30, 1989 (when applicable) that do not conflict with or contradict GASB pronouncements. The District has the option to apply FASB pronouncements issued after that date and has elected to apply those when applicable. The more significant accounting policies established in GAAP and used by the District are discussed below.

In June, 1999 the Governmental Accounting Standards Board (GASB) unanimously approved Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*. Certain of the significant changes in the Statement include the following:

- For the first time, GASB requires the financial statements to include:
 - A Management’s Discussion and Analysis (MD&A) section providing an analysis of the District’s overall financial position and results of operations. Management has elected to omit the Management Discussion and Analysis.
 - Financial statements are prepared using full accrual accounting for all of the District’s activities.

Financial Reporting Entity

The District’s basic financial statements include the accounts of all District operations. The District is a separate legal entity created by the Kansas Legislature as described above. As a result, the District is a special-purpose government engaged in a single governmental program.

Basis of Presentation

The statement of net assets reports information on all of the activities of the District. The statement of activities includes revenues and expenses related to the primary, continuing operations of the District. Principal operating revenues are charges to customers for sales or services. Principal operating expenses are the costs of providing goods or services and include administrative expenses.

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

NOTES TO FINANCIAL STATEMENTS
For the years ended December 31, 2012 and 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Measurement Focus/Basis of Accounting

Measurement focus refers to what is being measured; basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied.

The financial statements are reported using the economic resources measurement and the accrual basis of accounting. The economic resources measurement focus means all assets and liabilities are included on the Statement of Net Assets and the operating statement presents increases (revenues) and decreases (expenses) in net total assets. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized at the time the liability is incurred.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Cash and Cash Equivalents

Cash includes all monies in the bank that are not restricted by debt covenants, which are classified as noncurrent assets, and highly liquid investments with original maturity dates of less than three months. The carrying value of cash approximates fair value because of the short maturities of those financial instruments. The District had no noncash financing transactions nor made cash payments for income taxes.

Capital Assets

All capital assets are valued at historical cost. Depreciation is based upon the estimated useful lives of the assets, using the straight-line method. Expenditures for major renewals and betterments that extend the lives of property and equipment are capitalized. When assets are retired or otherwise disposed of, the assets and related accumulated depreciation are reduced and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is expensed as incurred.

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

NOTES TO FINANCIAL STATEMENTS
For the years ended December 31, 2012 and 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any borrowings used for the acquisition. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation or through external restrictions. The District had no restricted net assets at December 31, 2012 and 2011.

Income Taxes

The District is a quasi-municipal governmental unit that is exempt from federal and state income tax.

NOTE 2 – CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following:

| | 2012 | 2011 |
|--------------|-------------------|-------------------|
| Petty cash | \$ 200 | \$ 200 |
| Checking | 105,580 | 55,480 |
| Money Market | 362,320 | 416,202 |
| Total Cash | <u>\$ 468,100</u> | <u>\$ 471,882</u> |

NOTE 3 – ACCOUNTS RECEIVABLE

Collections of accounts receivable are generally current. At December 31, 2012 and 2011, there were minimal amounts of uncollected accounts due over ninety days. Uncollectible accounts are written off in the period they become worthless.

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

NOTES TO FINANCIAL STATEMENTS
For the years ended December 31, 2012 and 2011

NOTE 4 – CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2012 was as follows:

| | Balance January 1 | Additions/ Completions | Retirements/ Adjustments | Balance December 31 |
|---------------------------------------|----------------------|---------------------------|-----------------------------|------------------------|
| Capital assets not being depreciated: | | | | |
| Land | \$ 52,598 | | | \$ 52,598 |
| Capital assets being depreciated: | | | | |
| Water Distribution System | 1,307,700 | 6,947 | | 1,314,647 |
| Less accumulated depreciation | (807,143) | (36,509) | | (843,652) |
| Net Being Depreciated | 500,557 | (29,562) | - | 470,995 |
| Total Capital Assets | <u>\$ 553,155</u> | <u>(29,562)</u> | <u>-</u> | <u>\$ 523,593</u> |

Capital asset activity for the year ended December 31, 2011 was as follows:

| | January 1 | Completions | Adjustments | December 31 |
|---------------------------------------|-------------------|----------------|------------------|-------------------|
| Capital assets not being depreciated: | | | | |
| Land | \$ 52,598 | | | \$ 52,598 |
| Construction in Progress | 136,781 | | (136,781) | - |
| Capital assets being depreciated: | | | | |
| Water Distribution System | 1,144,497 | 163,203 | | 1,307,700 |
| Less accumulated depreciation | (765,398) | (41,745) | | (807,143) |
| Net Being Depreciated | 379,099 | 121,458 | - | 500,557 |
| Total Capital Assets | <u>\$ 568,478</u> | <u>121,458</u> | <u>(136,781)</u> | <u>\$ 553,155</u> |

Depreciation expense for years ended December 31, 2012 and 2011 was \$36,509 and \$41,745, respectively.

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

NOTES TO FINANCIAL STATEMENTS
For the years ended December 31, 2012 and 2011

NOTE 5 – DEPOSITS AND INVESTMENTS

The District has excess cash invested in a money market account at a local bank at December 31, 2012 and 2011.

K.S.A. 9-1401 establishes the depositories which may be used by the District. The statute requires banks eligible to hold the District's funds have a main or branch bank in the county in which the District is located, or in an adjoining county if such institution has been designated as an official depository, and the banks provide an acceptable rate of return on funds. In addition, K.S.A. 9-1402 requires the banks to pledge securities for deposits in excess of FDIC coverage. The District has no other policies that would further limit interest rate risk.

K.S.A. 12-1675 limits the District's investment of idle funds to time deposits, open accounts, and certificates of deposit with allowable financial institutions; U.S. government securities; temporary notes; no-fund warrants; repurchase agreements; and the Kansas Municipal Investment Pool. The District has no investment policy that would further limit its investment choices.

Concentration of credit risk. State statutes place no limit on the amount the District may invest in any one issuer as long as the investments are adequately secured under K.S.A. 9-1402 and 9-1405.

Custodial credit risk – deposits. Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to the District. State statutes require the District's deposits in financial institutions to be entirely covered by federal depository insurance or by collateral held under a joint custody receipt issued by a bank within the State of Kansas, the Federal Reserve Bank of Kansas City, or the Federal Home Loan Bank of Topeka, except during designated "peak periods" when required coverage is 50%.

The bank carrying amounts of the District's deposits was \$468,801 and \$475,973 at December 31, 2012 and 2011, respectively. Of these amounts, \$416,202 and \$362,320 were interest bearing accounts. At December 31, 2012 and 2011, \$250,000 of the bank balance was covered by FDIC insurance. At December 31, 2012 and 2011, \$279,043 and \$269,883, respectively, was covered by pledges securities held under joint custody receipts issued by a third-party bank in the District's name. The third-party bank holding the pledged securities is independent of the pledging bank. The pledged securities are held under a tri-party custodial agreement signed by all three parties: the District, the pledging bank, and the independent third-party bank holding the pledged securities. At December 31, 2012 and 2011, respectively, all deposits were insured. At December 31, 2012 and 2011, the bank balances in non-interest bearing accounts were \$106,481 and \$59,771, respectively.

NOTE 6 – RISK MANAGEMENT

The District is exposed to various risks of loss related to torts: theft of, damage to, and destruction of assets; errors and omissions; injuries to employees. The District purchases insurance to provide coverage for these risks. There were no significant reductions in insurance coverage from the prior year.

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

NOTES TO FINANCIAL STATEMENTS
For the years ended December 31, 2012 and 2011

NOTE 7 – BOND ISSUE COSTS

Bond issue costs at December 31, 2012 and 2011 consisted of the following:

| | 2012 | 2011 |
|--------------------------------|-------------|-----------------|
| Bond issue costs | \$ 12,888 | \$ 12,888 |
| Less: Accumulated amortization | (12,888) | (11,062) |
| Net Bond Issue Costs | <u>\$ -</u> | <u>\$ 1,826</u> |

NOTE 8 – BONDS PAYABLE – LONG TERM DEBT

In July of 2003, Rural Water District No. 2, Jefferson County, Kansas issued Kansas Rural Water Finance Authority Revenue Bonds, Series H, 2003, in the amount of \$265,000 for the purpose of refinancing the Rural Water Finance Authority Revenue Bonds, Series D, 1994 bonds. Interest rates range from 2.0% to 3.5% payable on June 1 and December 1, beginning June 1, 2004. Annual principal payments range from \$20,000 to \$55,000 starting June 1, 2004 through June, 2012. Revenues produced from the District's system are pledged as collateral against the bonds. The bonds are subject to optional redemption and payment prior to maturity, upon instructions from the District, as a whole at any time, or in part on any interest payment date, at par plus accrued interest thereon to the date fixed for redemption and payment. The balance due at December 31, 2011 was \$55,000. There was no balance due at December 31, 2012.

| Bond Issue | Date Issued | Original Amount | Out-standing 1-1-12 | Issued | Principal Payments | Out-standing 12-31-12 |
|------------|-------------|-----------------|---------------------|--------|--------------------|-----------------------|
| 2003-H | 7-15-05 | \$ 265,000 | \$ 55,000 | \$ - | \$ 55,000 | \$ - |

Interest expense on outstanding bonds totaled \$969 for the year ending December 31, 2012 and \$2,435 for the year ending December 31, 2011.

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

NOTES TO FINANCIAL STATEMENTS
For the years ended December 31, 2012 and 2011

NOTE 9 – DEFERRED LOSS ON REFUNDING

When the bonds in Note 8 were issued, they were used to refinance bonds previously issued. This resulted in a deferred loss on refunding. This loss is being amortized over the life of the new bonds. The deferred loss on refunding on the statement of net assets is comprised of the following:

| | <u>2012</u> | <u>2011</u> |
|--------------------------------|-----------------|-----------------|
| Deferred loss on refunding | \$ 12,453 | \$ 12,453 |
| Less: Accumulated amortization | <u>(12,453)</u> | <u>(10,689)</u> |
| Net deferred loss on refunding | <u>\$ -</u> | <u>\$ 1,764</u> |

NOTE 10 – NEW CONSTRUCTION

The District built a new building to serve as their office. The total cost of the building at completion was \$154,389 and was placed in service on January 11, 2011.

NOTE 11 – SUBSEQUENT EVENTS

The Organization adopted FASB ASC Topic 855, *Subsequent Events*. ASC 855 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Specifically, it sets forth the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements, and the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. The adoption of ASC 855 had no impact on the Organization's financial statements.

In accordance with ASC 855, the Organization evaluated subsequent events through February 11, 2013, the date these financial statements were available to be issued. There were no material subsequent events that required recognition or additional disclosure in these financial statements.

SUPPLEMENTAL INFORMATION

RURAL WATER DISTRICT NO. 2
JEFFERSON COUNTY, KANSAS

SCHEDULES OF OPERATING EXPENSES
For the years ended December 31, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|--------------------------|-------------------|-------------------|
| Asset improvement | \$ 25,451 | \$ - |
| Bad debts | - | 302 |
| Chemicals | 1,508 | 366 |
| Ditching | 19,119 | 240 |
| Dues and subscriptions | 790 | 873 |
| Insurance | 5,169 | 4,536 |
| Interest expense | 969 | 2,435 |
| Miscellaneous | 1,496 | 553 |
| Office & postage expense | 3,330 | 1,965 |
| Professional fees | 5,651 | 6,015 |
| Rental/stoarge expense | 60 | 420 |
| Repairs and maintenance | 10,700 | 22,603 |
| Salaries | 40,753 | 39,290 |
| Supplies | 10,237 | 8,510 |
| Payroll taxes | 3,158 | 3,045 |
| Other taxes | 823 | 136 |
| Property taxes | - | 30 |
| Water protection tax | 1,501 | 1,166 |
| Testing expenses | 1,028 | 904 |
| Travel | 50 | 100 |
| Utilities | <u>14,145</u> | <u>11,887</u> |
| Total Expenses | <u>\$ 145,938</u> | <u>\$ 105,376</u> |

See accompanying notes to financial statements